



## HOUSE BILL 235: Simplify Gift Tax

### BILL ANALYSIS

**Committee:** Revenue Laws Study Committee  
**Introduced by:**  
**Version:** First Edition

**Date:** January 24, 2007  
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Committee Counsel

**SUMMARY:** *This bill would simplify the State gift tax by eliminating the tax on many gifts, by eliminating different tax rates based on the relationship between the donor and donee, and by more closely tying the State gift tax to the federal gift tax. This bill would become effective for gifts made on or after January 1, 2008.*

**CURRENT LAW:** Under the North Carolina gift tax gifts not exceeding a value of \$12,000 from any particular donor to any particular donee are excluded from taxation<sup>1</sup>. In addition, several types of gifts, such as gifts to cover medical or educational expenses, gifts between spouses, or charitable contributions, are not subject to the gift tax. After applying these exclusions, gifts are taxed at varying graduated rates based on the relationship between the donor and the donee. Gifts that are made to lineal descendants, lineal ancestors, adopted children, or stepchildren are taxed at the lowest rates and are subject to a lifetime cumulative exemption of \$100,000. Gifts that are made to siblings, descendants of siblings, or aunts or uncles by blood are taxed at higher rates and do not enjoy the benefit of the exemption. Gifts that are made to other donees are taxed at the highest rates and do not enjoy the benefit of the exemption. Thus, North Carolina's gift tax rate structure favors transfers to children and parents by giving those transfers the lowest rates and an exemption and prefers transfers to other close family members over transfers to more distant relatives or to persons who are not related. Other than a change in the annual exclusion amount from a flat rate of \$10,000 to the amount of the annual exclusion amount set under the Code, the General Assembly has not enacted any major changes to the gift tax since before 1998.

North Carolina's gift tax is similar to the federal gift tax in some limited ways, but is extremely different in some other important ways. As with the North Carolina gift, the federal gift tax has an annual exclusion amount and excludes gifts to cover medical or educational expenses, gifts between spouses, and charitable contributions. However, the federal gift tax rate does not vary based on the relationship between the donor and donee. In addition, the federal gift tax is part of a somewhat unified gift-estate tax system at the federal level. As part of that system, the federal gift tax has a lifetime exemption amount of \$1,000,000. This amount is much larger than the State exemption amount and is available regardless of the relationship between the donor and donee. In addition, there are sometimes differences in the valuation of a gift for State and federal tax purposes. This most commonly occurs with respect to the valuation of annuities. For State purposes, statutes mandate an interest rate of 6% be used in determining the value of the annuity; for federal purposes, the current prevailing interest rate is used.

**BILL ANALYSIS:** This bill would more closely conform North Carolina's gift tax to the federal gift tax. This bill would include the following key changes:

- A State gift tax would be imposed only if a federal gift tax were imposed. This is similar to the manner in which the State imposes an estate tax. By imposing a State gift tax only when a federal gift tax is due, the practical effect is to greatly increase the lifetime exemption amount. A federal tax is only due once the taxpayer's lifetime taxable gifts have exceeded \$1

<sup>1</sup> The annual exclusion amount does not apply to gifts of a future interest.

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million; by imposing a State gift tax only when a federal tax imposed, the State effectively incorporates the \$1 million lifetime exclusion amount.

- The bill eliminates different treatment of gifts based on the relationship between the donor and donee. This bill would institute a single rate structure for all taxable gifts and would effectively incorporate a single lifetime exemption amount for all types of gifts.
- The bill would conform the valuation of gifts for State purposes to the valuation of gifts for federal purposes.
- The bill would conform the rate schedule for the State gift tax to the rate schedule for the State estate tax. In most cases, this would result in the taxpayer paying tax at a significantly lower rate.

**EFFECTIVE DATE:** This bill would become effective for gifts made on or after January 1, 2008.

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